Audit Manual

Chapter 5

Penalties

Sales and Use Tax Department
California State
Board of Equalization

This is an advisory publication providing direction to staff administering the Sales and Use Tax Law and Regulations. Although this material is revised periodically, the most current material may be contained in other resources including Operations Memoranda and Policy Memoranda.
Please contact any board office if there are concerns regarding any section of this publication.

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INTRODUCTION 0501.00

BOARD POLICY ON PENALTIES 0501.05

It is the policy of the Board to encourage and assist all taxpayers in making an accurate and timely self-declaration of their tax liability. When that is done, there should be no occasion for imposition of penalties for negligence or fraud. The Board recognizes the many difficulties that taxpayers may be confronted with in attempting to comply with all requirements of the law. While unduly rigid or exacting requirements are not in the best interest of good tax administration, the Board does not condone carelessness or deliberate disregard by taxpayers of their obligations to keep accurate records and prepare proper returns. *Whenever there is any doubt as to whether factual conditions warrant a penalty for negligence or fraud, that doubt should be resolved in favor of the taxpayer.* However, where penalties are justified by the acts or omissions of the taxpayer, they should be applied properly and impartially.

TYPES OF PENALTIES — OVERVIEW 0501.10

The Sales and Use Tax Law sections covered by this audit manual provide for several penalties. There are penalties that are mandatory and imposed automatically, such as those imposed because payments are late, without regard to whether an audit is performed. There are others that are discretionary and may be assessed by auditors in the conduct of their audits. The main penalties that auditors may assess are summarized as follows:

Nature of Penalty	Rate	Law Section
Failure to file a return	10%	6511
Negligence or intentional disregard of the laws or regulations	10%	6484
Fraud or intent to evade the law or regulations	25%	6485
Knowingly not obtaining a valid permit in order to avoid the tax	50%	7155
Improper use of a resale certificate for personal gain or to evade the tax	*	6072; 6094.5
Registration of vehicle, vessel, or aircraft out of state to evade the tax	50%	6485.1; 6514.1
Failure to obtain evidence that operator of catering truck holds valid seller's permit	$500	6074
Failure of retail florist to obtain permit	$500 **	6077

*10% of the tax due or $500 whichever is greater

**Plus any other applicable penalty

RESPONSIBILITY OF FIELD AUDITORS FOR PENALTY RECOMMENDATIONS 0501.15

Most negligence and fraud penalties are imposed as a part of the determinations based upon field audit recommendations. Field auditors and their supervisors are responsible for making sound penalty recommendations based upon factual findings. This requires good judgment, common sense and a thorough understanding of the penalty provisions of the law.

A negligence penalty and a fraud penalty can never apply concurrently. The two penalties are mutually exclusive. The same is true of the penalty for negligence and the penalty for failure to file a return. However, a fraud penalty and a 10% penalty for failure to file may be added to the same tax.

Whenever circumstances warrant the imposition of either a mandatory or a discretionary penalty, but not both, *the mandatory penalty will apply.* For example, the penalty for failure to file a return rather than the negligence penalty will apply in those cases where either penalty could be applied.

DELINQUENCY PENALTIES 0501.20

For taxpayers not paying their taxes by EFT when they are required to do so, Section 6591 of the Sales and Use Tax Law imposes a 10% penalty for failure to pay tax timely. On and after January 1, 1997, this section also imposes a 10% penalty for failure to file a timely return. For taxpayers paying their taxes by EFT, as of January 1, 1999, Section 6479.3 includes all EFT related penalties. The penalties imposed under either of these sections are limited to a maximum of 10% of the amount of taxes, exclusive of prepayments, for the reporting period.

Returns are considered to cover the period which is indicated on them. For example, a taxpayer on a monthly basis does not report sales for May, but instead includes these sales on his or her June return. The failure to file penalty would apply to May even though sales were subsequently reported in June.

Section 6476 imposes a 6 percent penalty on the amount of a prepayment that is paid late but which is paid before the last day of the monthly period following the quarterly period in which the prepayment was due.

Section 6477 imposes a penalty when a taxpayer fails to make a prepayment noted in the above paragraph but files before the last day of the monthly period following the quarterly period in which the prepayment became due, provided the taxpayer files a timely return and payment for the quarterly period in which the prepayment became due. The penalty is 6% of the amount equal to 90% of the tax liability for each of the periods during that quarterly period for which a required prepayment was not made.

The penalty imposed under section 6477 is increased by section 6478 to 10 percent if the failure to make the prepayment was due to negligence or intentional disregard of the Sales and Use Tax Law or authorized rules and regulations. Section 6478 also imposes a 10 percent penalty on the amount of any deficiency in the required prepayment if any part of that deficiency is the result of negligence or intentional disregard of the Sales and Use Tax Law or authorized rules and regulations. The penalties discussed in this paragraph are not applicable to amounts subject to a penalty under sections 6484, 6485, 6511, 6514, or 6591.

WAIVER OF MANDATORY PENALTIES 0501.25

The Board is empowered to relieve taxpayers of mandatory penalties for failure to file a timely return, payment, or prepayment when the Board determines that the failure was due to a reasonable cause and circumstances beyond the person's control and occurred notwithstanding the exercise of ordinary care.

Relief from penalties will be considered by the Board Members at their regular meetings. Taxpayers wishing to request relief should do so after issuance of a determination. A request for relief must be presented in a written statement, under penalty of perjury, setting forth the facts upon which the request is based.

PENALTIES FOR NEGLIGENCE AND FRAUD 0501.30

These penalties are imposed when there is "negligence or intentional disregard" or "fraud or intent to evade" the law or rules and regulations, and may be asserted only as a part of determinations made by the Board under the laws. Such penalties may be protested and are subject to cancellation if they subsequently are found to have been asserted in error.

On July 19, 1944, the Board ordered that when a "fraud" or "intent to evade" penalty has been imposed (i.e., billed on a Notice of Determination), any change in such penalty shall be made only by the elected Board itself and not by Board staff.

PENALTIES IN BANKRUPTCY CASES 0501.35

In bankruptcy cases, penalties are chargeable to the various parties involved, as indicated below. It will be noted that these instructions also apply to debtors in possession under Chapters X and XI of the Bankruptcy Act.

Section 507(a)(8) of the Bankruptcy Code does not permit a tax penalty to be filed as a priority claim against the bankrupt estate in regular bankruptcy proceedings. Accordingly, no penalties attaching under any of the provisions of the business tax laws can be included in the priority claim against the bankrupt estate in such proceedings. However, the penalties become the personal liability of the debtor, whether attaching before or after the date of the petition in bankruptcy, unless chargeable against a trustee, receiver or "debtor in possession" or unless corporate reorganization or arrangement proceedings are involved. Any appropriate penalties should be included when submitting Form BOE–414–A so that steps may be taken to collect such penalties under personal liability of the debtor after discharge.

RECEIVERS, TRUSTEES AND DEBTORS IN POSSESSION 0501.40

Receivers or trustees of bankrupt estates and debtor in possession under Chapter X or XI are liable for penalties incurred while operating the bankrupt business. Accordingly, penalties which attach by reason of the delinquency or misfeasance of a receiver, trustee, or debtor while operating the bankrupt business will be billed against such receiver, trustee, or debtor.

NEGLIGENCE AND EVASION PENALTIES — DECEASED TAXPAYERS 0501.45

Negligence and evasion penalties will not be included in determinations made after the death of an individual taxpayer. It is obvious that the malfeasant in such cases would not suffer the penalty, but the effect would be to reduce the assets for distribution to the estate of the deceased. However, such penalties are applicable to the negligence or evasion of the administrator(s) or executor(s) of the decedent's estate.

NEGLIGENCE AND EVASION PENALTIES — DEATH OF PARTNER 0501.50

If a partnership is properly subject to a negligence or evasion penalty, that penalty will still be imposed even if the partnership is thereafter dissolved due to death of one of the partners.

ASSIGNMENT FOR THE BENEFIT OF CREDITORS 0501.55

Any person who makes an assignment for the benefit of creditors and who owes an amount which became delinquent either before or after the assignment was made is charged with penalty and interest, when applicable, the same as other taxpayers.

LOCAL AND TRANSACTIONS TAXES 0501.60

The penalty provisions of this chapter also apply to Uniform Local Sales and Use Taxes and Transactions (Sales) and Use Taxes. The penalties for negligence and evasion normally will apply to state, local, and transactions taxes. However, a recommendation for penalty may be restricted to state tax and not local tax, and not transactions tax, or any combination, as appropriate.

DELINQUENCY PENALTIES 0502.00

WHEN PENALTY ATTACHES 0502.05

Delinquency penalty attaches if tax is not paid, as follows:

a) To self-declared tax, on or before the due date of the return or before the expiration of any extension that has been granted.

b) To determinations made by the Board, on or before the penalty date shown on the Notice of Determination unless a timely petition has been filed.

c) To redeterminations, on or before the penalty date shown on the Notice of Redetermination.

REPORTING BASIS 0502.10

Sales tax returns are due on a calendar quarterly basis unless the Board has required or allowed the taxpayer to file returns on another reporting basis. A taxpayer cannot retroactively be placed on a reporting basis shorter than its current reporting basis and become subject to a penalty for late payment because the due date for paying tax under the new reporting basis has already passed. Similarly, a taxpayer who has incurred a late payment penalty cannot avoid that penalty by being retroactively placed on a longer reporting basis.

DUE DATES OF RETURNS 0502.15

Due dates for returns filed on the various reporting basis are as follows:

Quarterly Basis

Returns are due on or before the last day of the month following the close of the quarter. Taxpayers who make prepayments must also file the prepayment returns in accordance with Section 6472.

Odd Quarterly Basis

Where sales tax accounts are reporting on a special basis which approximates that of the regular quarterly basis, such as a 13-month year, returns are due on or before the last day of the month following the close of the authorized reporting period.

Monthly Basis

Sales tax returns for each month are due on or before the last day of the following month.

Yearly Basis

Returns are due on or before the last day of the month following the close of the calendar year (reporting basis Y) or fiscal year (reporting basis F), except when the taxpayer closes out before the end of the year. (See Section 0502.30.)

When changing an account from a yearly or fiscal year basis to another basis, and the effective date is other than the beginning of the yearly reporting period, the district will furnish the taxpayer with a return to report the expired portion of the year to and including the last day of the quarter which precedes the effective date of the new basis. The tax return for the expired portion of the year is due on or before the last day of the month following the effective date of the new basis.

SALES TAX LIABILITY OF PURCHASERS 0502.20

A purchaser who becomes liable for payment of sales tax as if he or she were a retailer making a retail sale under Section 6421 of the Sales and Use Tax Law has an obligation to file returns and is subject to the failure to file penalty provisions of Section 6511.

CLOSEOUTS 0502.30

Except for taxpayers on an annual reporting basis, if a taxpayer sells a business or stock of goods or quits the business, a final return is not due until the due date of the return for the taxpayer's reporting period during which the closeout occurred. For a taxpayer on an annual reporting basis who closes out the business, a closing return is due on or before the last day of the month following the close of the quarterly period in which business was discontinued.

EFFECT OF LEGAL HOLIDAYS AND WEEKENDS ON DUE DATES 0502.35

Whenever the due date of the tax falls on a Saturday, Sunday, or legal holiday, the tax may be paid on the following business day without penalty. The following is a list of legal holidays as set forth in the Government Code:

New Year's Day	January 1
Martin Luther King, Jr. Day	3rd Monday in January
Lincoln's Birthday	February 12
President's Day	3rd Monday in February
Memorial Day	Last Monday in May
Independence Day	July 4
Labor Day	1st Monday in September
Columbus Day	2nd Monday in October
Veterans Day	November 11
Thanksgiving Day and Day After	4th Thursday and Friday in November
Christmas	December 25
Every day appointed by the President of the United States or by the Governor of this State for a public fast, thanksgiving, or holiday.	

If one of the foregoing legal holidays falls on a Sunday, the following Monday is a legal holiday.

If Veteran's Day falls on a Saturday, the preceding Friday is a legal holiday

STATUTORY DATE FALLING ON SATURDAY, SUNDAY OR HOLIDAY 0502.36

Actions other than filing and paying returns, which must be timely, include:

1) Waiving the statute of limitations (Section 6488)
2) Filing a petition for redetermination (Section 6561)
3) Filing a claim for refund (Section 6902)
4) Filing a suit for refund (Sections 6933 & 6934)
5) Issuing a determination (Section 6487)

The first four of these acts are permitted by taxpayers, and the last is a duty imposed on the Board. All of the acts are required by statute to be performed within a specified period of time.

When the due date of these acts falls on a Saturday, Sunday or holiday, it will nevertheless be timely if filed on the next business day that is not a legal holiday.

PETITIONS FOR REDETERMINATION 0502.45

A penalty is imposed on the amount of any determination made by the Board which is not paid on or before the date indicated on the notice, unless a petition is filed on or before that date. The rules for determining when a petition was filed are the same as those for determining when a payment was made.

In preparing a reaudit, the auditor should determine if the petition was timely. The taxpayer should be notified of any penalty to be added by headquarters because of a late protest or payment. Comments on the audit report should also indicate that a penalty will be added by headquarters.

PAYMENTS OR PETITIONS MAILED BUT NOT RECEIVED 0502.50

For purposes of determining whether a late payment or late filing penalty is applicable or a petition is filed timely, a payment or a petition alleged to have been placed in the mail will generally not be treated as received or filed timely unless it is actually received by the Board. Exceptions will be made in those instances where the taxpayer furnishes satisfactory proof that the original payment or petition was mailed timely.

JEOPARDY DETERMINATIONS 0502.55

Jeopardy determinations become final within 10 days after service of notice unless a petition is filed within such period and security is deposited in such amount as the Board may deem necessary. The Board will not recognize a petition in connection with a jeopardy determination unless such security is deposited with the Board on or before the date on which penalty attaches, in one or more of the following forms:

1) Cash deposits (personal checks not acceptable).
2) Certificates of deposit issued by banks.
3) Savings and loan certificates.

A document that purports to be a petition filed in connection with a jeopardy determination where security is not deposited is not a valid petition.

EXTENSIONS FOR FILING RETURNS 0502.60

The various business tax laws provide in part:

> "The Board for good cause may extend for not to exceed one month the time for making any return or paying any amount required to be paid under this part. The extension may be granted at any time provided a request therefor is filed with the Board within or prior to the period for which the extension may be granted."

Extensions are granted by the appropriate headquarters unit only and must be requested by the taxpayer. Generally, the taxpayer requests the extension from the district office and the district office will submit a recommendation the appropriate unit. When an extension is granted for a specific period, a delinquency penalty will not apply if the tax is paid on or before the last day of the period for which the extension was granted. However, when an extension is granted, interest from the date on which tax would have been due must be paid. In cases in which an extension of time has been granted for making a prepayment, interest applies to the unpaid amount of the required prepayment.

PENALTY FOR FAILURE TO FILE A RETURN 0503.00

WHEN PENALTY APPLIES 0503.05

Each taxpayer who has an active account under any of the revenue laws administered by the Board is required to file returns at regular intervals as prescribed by law and required by the Board. The 10% penalty for failure to file a return is imposed on the amount of taxes due, exclusive of prepayments, with respect to the period for which that return was required. (Also discussed in section 0501.20.) If the taxpayer is on a monthly reporting basis, for example, and failed to file a return for only one month during a period under audit, a penalty would apply only to tax due for that month. Generally, the appropriate headquarters unit determines whether a return has been filed for a given period at the time Form BOE–414 is prepared. Section 6487 provides the statute of limitations on issuing determinations for failure to file a return. Under this section, a determination must be mailed within eight years after the last day of the calendar month following the quarterly period for which the amount is proposed to be determined.

The field auditor should be familiar with the following rules relating to this type of penalty.

DEFINITION OF A RETURN 0503.10

A return may be defined as a report filed with the Board by the taxpayer, in such form as may be prescribed by the Board, showing the amount of taxes due for the period covered.

WHAT CONSTITUTES FILING A RETURN OR REPORT 0503.15

A return is considered filed when the taxpayer provides in writing:

(a) A request that the correspondence be accepted as a return or statement, regardless of how brief, indicating that the taxpayer is attempting to file a return.

(b) The reporting period for which the correspondence (return) is filed.

(c) The amount of tax due or that no tax is due.

When the taxpayer has shown due diligence in making every effort to submit what he or she feels is a return, the correspondence submitted should be accepted as a return. Even if the correspondence has no gross sales or deductions and shows only the net tax figure, it may be accepted as a return if the information listed above is provided. If a taxpayer's check indicates the reporting period and the measure of the tax being paid, it may be processed as a return. As a general rule, if tax due can be calculated from the information provided, the correspondence should be processed as a return. It is important to always consider the taxpayer's intent.

FORM BOE–401–E NOT A RETURN FOR ALL PURPOSES 0503.20

The filing of a Form BOE–401–E, Consumers Use Tax Return, cannot be regarded as the filing of a return with respect to sales tax liability as a seller, or use tax liability as a retailer, but only as the filing of a return with respect to use tax liability as a purchaser.

UNSIGNED NO-REMITTANCE RETURNS 0503.25

When a document is received purporting to be a tax return, either on one of the forms prescribed by the Board or on some other form, which is not signed by the taxpayer and is not accompanied by a remittance, it will not be regarded as a return.

CLOSEOUTS WITH SECURITIES 0503.30

A cash deposit, certificate of deposit, or an insured deposit in a bank or savings and loan institution is considered to be an advance payment of any tax due on or after the date of closeout. This security will be applied in accordance with the guidelines discussed in the Compliance Policy and Procedures Manual (Section 400.000).

A negligence, fraud, or intent to evade penalty does not apply to a deficiency that is paid by the application of a liquid security where the due date is on or after the closeout. This is because there was no amount required to be paid to which the penalty can be added. If the taxpayer is on a monthly basis, the quarter or quarters in which the closing month and the preceding month, if involved, occur should be segregated on Form BOE–414–A1 in order to show clearly the application of cash deposit and penalties. In contrast, a penalty for failure to file will apply if a taxpayer submits a late return even though available security exists. Additionally, even if security is available to clear delinquent reporting periods for closed out accounts, the 10% failure to file penalty will apply. A note is added on the billing to inform the taxpayer regarding the penalty.

When the security is not sufficient to meet the liability for the closing period the procedure is as follows:

(a) When a return was filed —

Headquarters will issue a Form BOE–1210, Demand for Payment, or Form BOE–1210–1, Statement of Account, for the tax, interest, and penalty. Form BOE–414–A, Report of Field Audit, will not recommend a penalty because of failure to file but may recommend a penalty for negligence.

(b) When no return was filed —

Form BOE–414–A will include the penalty for failure to file for the amount of the taxes, exclusive of prepayments, with respect to the period for which the return is required.

When an audit is not to be made, attempts should be made to secure signed returns for periods for which no returns were filed. When the delinquent return or returns cannot be secured, a Form BOE–414–B, Field Billing Order, or Form BOE–10, Field Determination, will be prepared to cover the estimated liability.

A notation on BOE–414–A under “Special Instructions” should be made when a security is available. See Section 0204.12.

ERRONEOUS REFUNDS OF CASH DEPOSITS 0503.35

If a cash deposit available on the close-out date is erroneously refunded instead of being applied to a liability, no penalty or interest will be added to the amount which should have been paid from the cash deposit where these charges would have accrued solely because of the erroneous refund. In cases where nothing is owing at the time a refund is made and a liability is later developed, through an audit for example, a penalty and interest charge will be added.

NO RETURNS FILED FOR PERIOD PRECEDING CLOSING PERIOD 0503.40

There may be instances where no return was filed for the reporting period immediately preceding the closing period, and where the due date for the preceding period is after the date of closeout (e.g., the second quarter 1999, when close-out date was July 13, 1999). If any part of the liquid deposit is applied to tax due for such periods, a negligence penalty will not attach to the amount of tax so paid. The liquid deposit is considered available on the date of closeout. Therefore, to the extent that it is so applied, there is no amount required to be paid to the State to which penalty can be added. However, if a taxpayer fails to file a timely return for the preceding period, a failure to file penalty will apply to the amount of taxes, exclusive of prepayments, for this period that the return is required.

TAXPAYERS ON A MONTHLY BASIS 0503.45

In the case of taxpayers reporting on a monthly basis, where no return was filed for the closing month or the preceding month, the quarter or quarters in which such months occur should be broken down on Form BOE–414–A1, in order to show clearly the application of liquid deposit and penalties.

AVAILABILITY OF SECURITY BETWEEN BUSINESS TAXES 0503.55

All or the remainder of the security of a taxpayer's account may be transferred to another account of the same taxpayer. Information relative to the transfer is contained in the Compliance Policy and Procedures Manual (Section 400.0000).

MORE THAN ONE LOCATION 0503.65

Sellers engaged in business at more than one location must hold a permit for each location, or a subpermit for each location under a consolidated account.

However, taxpayers who hold seller's permits for permanent places of business, and also conduct operations of a temporary nature at places such as fairs or carnivals, are not required to hold separate permits for the temporary operations. They should report their sales made at the temporary location with the returns filed under their regular permit numbers. For multiple location permits, the temporary locations should be listed on BOE–530, "Schedule C — Detailed Allocation by Suboutlet of Uniform Local Sales and Use Tax." For single location permits, the temporary locations should be listed on BOE–530–B, "Local Tax Allocation for Temporary Sales Locations and Certain Auctioneers." The three-year limitation period applies, and the penalty for failure to file returns does not apply, with respect to any unreported sales tax liability incurred at the temporary location during any period for which a person has filed a return for a permanent place of business.

The three-year limitation period applies, and the penalty for failure to file returns does not apply, with respect to any unreported sales or use tax liability incurred in any period for which a person has filed a return for any location. This is true even though the person may operate at one or more other locations for which neither a permit nor a subpermit has been issued.

Where a taxpayer operating under a consolidated permit fails to include sales in his or her return relating to business at a particular location for which a subpermit is held, a penalty for failure to file a return does not apply, but the ten percent penalty for negligence or the 25 percent penalty for fraud may apply if circumstances warrant.

NEGLIGENCE PENALTIES — GENERAL 0504.00

LEGAL BASIS 0504.05

The sections relating to the negligence penalty contain the following language:

> "If any part of the deficiency for which a deficiency determination is made is due to negligence or intentional disregard of this part or authorized rules and regulations, a penalty of 10 percent of the amount of the determinations shall be added thereto."

DEFINITION 0504.10

Negligence may be defined in general as a failure to exercise due care. In most cases, the law has defined the exercise of due care as such care that a reasonable and prudent person would exercise under similar circumstances. With respect to business tax matters, negligence may be further defined as a substantial breach by the taxpayer of some duty imposed by the law or authorized rules and regulations.

NEGLIGENCE VS. INTENTIONAL DISREGARD 0504.15

There may be a technical distinction between negligence and intentional disregard of the law or authorized rules and regulations in that intentional disregard implies something more than negligence. However, intentional disregard is less than fraud or an intent to evade the tax and is covered by the negligence penalty. Accordingly, the term "negligence penalty" will be used to include the penalty for negligence or for intentional disregard. If, however, a situation is encountered where the field auditor believes there is strong evidence of intentional disregard of the law or authorized rules and regulations, the audit report should include appropriate comments regarding the evidence of intentional disregard.

Field auditors should not assume that a large audit deficiency or overpayment is indicative of either negligence or intentional disregard. As stated in section 0101.20, the auditor is to use his or her highest skill and best judgment to determine whether the amount of tax has been reported correctly. This same judgment and skill should be used to determine whether a penalty should or should not be recommended. As detailed in section 0504.35, a recommendation must be supported by appropriate comments.

ACTS OF AN AGENT, EMPLOYEE OR PARTNER 0504.20

In general, where an agent, employee, or partner of the taxpayer is guilty of negligence, with a resulting tax deficiency, the 10 percent penalty will apply. This is true even though the agent, employee, or partner acted without the taxpayer's knowledge or consent, or acted contrary to the express instructions of the taxpayer. Situations may be encountered where the taxpayer has been defrauded by an agent, employee, or partner and as a result did not benefit from the understatement of tax. Whether the negligence penalty is imposed will depend upon whether circumstances made it difficult or impossible for the taxpayer to detect such fraud.

CONDITIONS UNDER WHICH PENALTY APPLIES 0504.25

The negligence penalty applies only to deficiency determinations and it applies to the total amount of the tax deficiency. In the normal field audit, this will mean that, if the penalty applies, it will be for the entire period of the audit regardless of class of transactions involved. Before the penalty is warranted, the following conditions must be present:

a) A tax deficiency, and

b) Evidence that any part of the tax deficiency is the result of negligence (or intentional disregard of the law or authorized rules and regulations).

IF APPLICABLE TO ONLY PART OF PERIOD 0504.30

Situations may be encountered where the condition warranting the imposition of a negligence penalty is not present during the entire period under audit and where the imposition of the penalty to the entire amount of the tax deficiency would be inequitable. For example, a complete change of management occurred and conditions under one management were entirely different from those under the other. In these situations, a full statement of the facts involved should be incorporated in the field audit report, and headquarters office will make two determinations, one for the period during which the 10 percent penalty should be included, and another for the period during which it should not be applied. Two Forms BOE–414–A will be required in such cases. When considering the recommendation to impose a negligence penalty on a partial audit period, auditors should determine if the taxpayer made any effort during a subsequent period in the audit to correct the situation which led to negligence. If such an effort has been made, a penalty may not be appropriate.

PENALTY COMMENTS ON AUDIT REPORTS OR FBOS 0504.35

Section 0206.03 states that "a comment should be made on any point which will be of value in connection with making a determination" or in "making a decisions respecting future audits." Penalty recommendations are frequently a source of disagreement between staff and taxpayers. To ensure that both staff and taxpayers understand why a negligence penalty was or was not recommended, a penalty comment using the following guidelines *must* be made on the back of the Form BOE–414–A or BOE–414–B. The *sole* exception is when the tax liability is less than $2,500 and no penalty is recommended.

The factors which constitute negligence in keeping records (discussed in section 0505.00), negligence in preparing returns (discussed in section 0506.00), and evasion penalties (discussed in section 0507.00), must be carefully considered before determining whether a negligence or evasion penalty should be imposed. If a negligence penalty is being recommended, the auditor must provide in clear and concise terms the rationale for imposing a penalty. An explanation of the evidence and facts upon which the auditor relies to support the recommendation for imposition of a penalty must be given. The explanation must enable supervisors and other reviewers to determine whether the recommendation is consistent with the facts established by the audit. The comments must be factual, not the auditor's opinion, and must not be derogatory to the taxpayer or the taxpayer's employees. All penalty comments must be sufficiently clear to provide continuity for subsequent audits of the taxpayer.

If the auditor believes the imposition of a penalty is inappropriate, he or she must use the same penalty comment guidelines as when recommending a negligence penalty. That is, the comments must be clear and concise, they must enable supervisors and other reviewers to determine whether the recommendation is consistent with the facts established by the audit, and they must be sufficiently clear to provide continuity in the event of a subsequent audit. Canned comments such as "Negligence not noted;" "No negligence noted;" or "No penalty recommended," are **not** acceptable.

If an evasion (fraud) penalty is being recommended, the comment on the audit report must be to the effect that, "Penalty pursuant to Sec. 6485 of the Sales and Use Tax Law is recommended." The details to support the recommendation will be included in the memorandum required by section 0507.75.

PENALTY COMMENTS ON AUDIT REPORTS OR FBOS 0504.35

Field auditors are frequently faced with the decision of whether to recommend a penalty on the first audit of a taxpayer. This decision must be based on an objective evaluation of the audit findings and the taxpayer's background and experience. Generally, a penalty should not be recommended. However, there are circumstances where a penalty would be appropriate. Criteria that should be considered, among others, are the taxpayer's prior business experience, the nature and state of the records provided, and whether the taxpayer used an outside accountant or bookkeeper to compile and maintain the records. For example, a penalty may be appropriate in any of the following circumstances: the taxpayer has no records of any kind, the taxpayer has a history of prior permits or business experience, analysis shows that purchases have exceeded reported sales, the taxpayer has two sets of books. The comment "Taxpayer's first audit" should only be used in conjunction with a detailed explanation for the penalty recommendation.

To promote consistency in the application of penalties and the writing of penalty comments, all comments must be reviewed by the auditor's supervisor. In addition, special procedures will be used for the following reviews:

- **Audit tax deficiency over $25,000** — Reviewed and approved by the auditor's supervisor
- **Audit tax deficiency over $50,000** — Reviewed and approved by the District Principal Auditor in addition to the auditor's supervisor.

This review and approval must be noted by the supervisor (and DPA if applicable) by commenting and signing directly below the auditor's penalty comment on the back of the BOE–414–A or BOE–414–B. This may be a handwritten comment or incorporated as the last line of the penalty comment (e.g., "Reviewed and approved. _____, Supervisor;_____, DPA.")

CLASSES OF NEGLIGENCE 0504.45

A taxpayer may be negligent in a number of ways, but there are only two kinds of negligence which will result in a tax deficiency and which may warrant the imposition of the negligence penalty. These are:

a) Negligence in keeping records, and

b) Negligence in preparing returns.

NEGLIGENCE IN KEEPING RECORDS 0505.00

GENERAL 0505.05

Guidelines for the maintenance of records are provided by Regulation 1698, *Records*. In general, this regulation provides that "a taxpayer shall maintain and make available for examination on request by the Board or its authorized representative, all records necessary to determine the correct tax liability under the Sales and Use Tax Law and records necessary for the proper completion of the sales and use tax return." Such records include:

- Normal books of account ordinarily maintained by the average prudent business person engaged in the activity in question.
- Bills, receipts, invoices, cash register tapes, or other documents of original entry supporting the entries in the books of account.
- Schedules or working papers used in connection with the preparation of tax returns.

Complete absence of records will constitute strong evidence of negligence. However, auditors should determine if there are mitigating circumstances for the lack of records (See section 0505.50). Where records are maintained and a tax deficiency results, various factors must be taken into consideration in determining whether the tax deficiency was due to negligence in keeping records. The term "records" as used herein includes not only those specifically mentioned in Regulation 1698, but also such supporting data as resale certificates, shipping documents in support of interstate transactions, etc.

TEST FOR NEGLIGENCE IN KEEPING RECORDS 0505.10

The primary test for negligence is whether a taxpayer keeps the type of records ordinarily maintained by a reasonable and prudent businessperson with a business of similar kind and size. If the evidence indicates that a taxpayer failed to keep such records and, as a result, failed to compile his or her tax returns with a reasonable degree of accuracy, and cannot substantiate the reported amounts when audited, negligence is indicated and the 10 percent penalty may be appropriate.

RECORDS NEED ONLY BE ADEQUATE FOR TAX PURPOSES 0505.15

Records need only be adequate for tax purposes. The fact that the records may not be adequate for the purpose of preparing balance sheets or profit and loss statements, or for furnishing accurate cost data, information to stockholders, creditors, or others interested in the business does not constitute negligence for tax purposes.

RECORDS NEED ONLY BE ADEQUATE FOR TYPE OF BUSINESS 0505.20

Records need only be adequate to meet the tax requirements of the type of business involved. For example, a small restaurant may require a very simple set of records for sales tax purposes, whereas, a large department store, oil company, automobile dealer, or contractor will require a much more complex accounting system.

NEGLIGENCE OF OTHER TAXPAYERS — NO EXCUSE 0505.25

A taxpayer should not be relieved of penalty for negligence in keeping records merely because there are many other taxpayers engaged in the same kind of business who also are negligent in keeping records. Each individual case should be decided on its own merits.

EFFECT OF LACK OF KNOWLEDGE ON PART OF TAXPAYER 0505.30

A taxpayer should not be relieved of a penalty for negligence in keeping records merely because he or she is unaware of the requirements of the law. However, while lack of knowledge is no defense to the negligence penalty, a taxpayer of little education should not be expected to keep records in as good a form as a taxpayer who has wide knowledge of correct accounting principles. The taxpayer, moreover, cannot be regarded as negligent merely because his or her records may be kept in a foreign language.

ERRORS IN KEEPING RECORDS 0505.35

Where records are adequate for tax purposes but numerous errors have been made which result in understatements of tax, the test for negligence is whether or not the taxpayer exercised due care in keeping the records.

ERRORS DO NOT NECESSARILY CONSTITUTE NEGLIGENCE 0505.40

No matter how carefully records are prepared and checked, some errors may occur. Accordingly, where errors are made in keeping records, the relative frequency and importance thereof must be considered before a taxpayer may properly be regarded as negligent. Due consideration should be given to any particular accounting difficulties which may be inherent in the taxpayer's business.

CONSIDERATIONS IN CLASSIFYING ERRORS 0505.45

To determine whether errors constitute negligence, the following should be considered:

a) The frequency of the errors relative to the volume of transactions. The number of errors found must be considered in relation to the total number and dollar amount of the same type of transaction in the audit period.

b) The ratio of understatement to reported amounts. This ratio may be used in a variety of ways. For markup audits, the most appropriate evaluation is the ratio of understatement to reported taxable measure, particularly when reported taxable sales have been impeached. For audits where taxable measure is based on a percentage of total sales or claimed deductions, the most appropriate evaluation is the measure of understatement to total reported sales or claimed deductions. For both of these methods, a large ratio of understatement may be indicative of negligence. If the audit measure is derived from a statistical sample, comparison of the error percentage in the prior audit may be appropriate if the same items are being sampled. A substantive increase or comparable error percentage may be indicative of negligence. However, it must be noted that a ratio of understatement is not, in and of itself, proof of negligence. A ratio should be considered in conjunction with other factors to determine whether negligence has occurred.

c) The probable cause. Auditors should consider the probable cause of errors found by audit. The cause of errors may result from procedural or operational problems unrelated to negligence. For example, significant changes in sales volume from a prior audit may cause errors that result from staffing problems rather than negligence. Similarly, a business with a large volume of small dollar transactions may find it infeasible to hire the level of staff that would result in the total elimination of errors.

If the errors are too frequent in relation to the volume of transactions, or if they result in a higher ratio of understatement than would be expected of a reasonable and prudent businessperson engaged in a business of similar kind and size, or if there appears to have been an absence of due care, the 10 percent penalty should apply.

DESTRUCTION OF RECORDS 0505.50

All records pertaining to transactions involving sales or use tax liability must be preserved for a period of not less than four years unless the Board authorizes in writing their destruction within a lesser period.

Whether unauthorized destruction of records constitutes negligence depends on the circumstances in each case.

Where Records Accidentally Destroyed

When the taxpayer has exercised due care in preserving the records, but they have been accidentally destroyed in spite of such care, the taxpayer cannot be said to have been negligent in failing to retain records. In reaching such a conclusion, the auditor should be satisfied that the records were actually destroyed, and that the destruction was accidental.

Where Records Intentionally Destroyed

Where records have been intentionally destroyed or destroyed as a result of negligence or lack of due care on the part of the taxpayer, any tax deficiency that is established will be presumed to have been the result of the taxpayer's negligence in destroying the records. The 10 percent penalty will apply unless there is evidence that the deficiency is not the result of the destruction of the records.

NEGLIGENCE IN PREPARING RETURNS 0506.00

DEFICIENCY DUE TO MISUNDERSTANDING 0506.05

Where there is evidence that the tax deficiency resulted from a reasonable misunderstanding by the taxpayer concerning the application of the tax, no penalty will apply. However, where the taxpayer has been advised, as a result of a prior audit or by other means such as a specific letter, documented telephone call, or special industry notice, that the unreported items were subject to the tax, it is indicative of intentional disregard and a penalty may apply. The 10 percent penalty should not apply when there are mitigating circumstances such as an attempt on the part of the taxpayer to report the items, or changes in the taxpayer's type of business or business operations that affected reporting of the transactions in question.

TEST FOR NEGLIGENCE IN PREPARING RETURNS 0506.10

As in the case of negligence in keeping records, the test for negligence in preparing returns is whether the taxpayer failed to exercise that degree of care which would be exercised by the ordinary prudent businessperson who is engaged in a business of a similar kind and size, and who in good faith has attempted to prepare returns with a reasonable degree of accuracy.

MECHANICAL ERRORS 0506.15

Mechanical errors in compiling returns do not constitute negligence unless they are sufficiently frequent or sufficiently large in amount to meet the test for negligence.

ERRORS IN APPLICATION OF LAW 0506.20

Errors in application of law when completing returns do not constitute negligence unless there is evidence that the taxpayer failed to exercise due care in determining whether the transactions in question were subject to tax. This can be determined by ascertaining whether the taxpayer has acted in good faith and has made a reasonably diligent effort to learn how the tax applies to his or her business. The average taxpayer is neither a lawyer nor an accountant and can only be expected to exercise the amount of diligence due from a businessperson in his or her circumstances.

DUTY TO MAKE INQUIRY 0506.25

Where there is doubt concerning the correct application of the tax, the taxpayer has a duty to make an inquiry. If the taxpayer fails to make an inquiry, the 10 percent penalty may apply. If the taxpayer does make an inquiry and fails to act upon the results of the inquiry, the 10 percent penalty generally should apply.

EFFECT OF ERRONEOUS INFORMATION 0506.30

If a taxpayer was in doubt as to the application of the tax, made an inquiry, was misinformed, and underreported tax based on that misinformation, the negligence penalty should not be imposed if the inquiry was made in good faith to any of the following:

a) The headquarters office,

b) The district office,

c) Any representative of the Board who is held out to the taxpayer as qualified and was authorized to give an opinion.

The taxpayer is required to furnish reasonable proof that the underreported tax was the result of erroneous information from the Board. In addition, the taxpayer should furnish a written statement of his or her interpretation of the information secured from the above sources.

Relief from application of a negligence penalty is based on a finding that there was actually no negligence and it should not be confused with relief under section 6596. Relief under section 6596 includes relief from tax, interest, and penalty where there has been written advice by the Board in response to a request in writing from a specifically identified taxpayer who, in turn, described fully the specific facts and circumstances of the activity or transaction for which advice was requested. Approval of a section 6596 credit or adjustment has been delegated by the elected Board to the Deputy Director, Sales and Use Tax Department, or his or her designee.

FAILURE TO REPORT PURCHASES SUBJECT TO USE TAX 0506.35

The same standards which determine the application of the negligence penalty to tax deficiencies arising from an understatement of gross receipts or an overstatement of deductions are used to determine the application of the negligence penalty to a tax deficiency arising from failure to report purchases subject to use tax.

MORE THAN ONE LOCATION 0506.40

A taxpayer operating under a consolidated permit who fails to include on returns sales relating to a location for which a subpermit is held may be presumed to be negligent for all tax due for that sublocation unless such omissions are infrequent and do not constitute a substantial part of the total deficiency.

OTHER TYPES 0506.45

While the two foregoing are rather obvious classes of negligence in preparing returns, it is not intended that the imposition of the penalty for this reason be so limited, since many other types of situations will be encountered where items have been omitted from returns for no apparent reason except that taxpayer was negligent.

WHERE WORKING PAPERS ARE DESTROYED 0506.50

Where the auditor finds that working papers used by the taxpayer in preparation of the tax returns have been destroyed and the taxpayer is unable to explain substantial deficiencies in reporting, taxpayer should be given a reasonable opportunity to prepare new working papers or to explain how amounts reported on returns were computed. Failure or inability on the part of the taxpayer to do so will ordinarily constitute evidence of negligence and warrant the imposition of the 10 percent penalty.

EVASION PENALTIES 0507.00

GENERAL 0507.05

Penalties for fraud or intent to evade are imposed only in connection with deficiency determinations made by the Board. *It is important to remember that the Board has the burden of supporting the imposition of an evasion penalty.*

Sections of the Sales and Use Tax Law dealing with such penalties are:

a) **Sections 6072 and 6094.5** — misuse of resale certificate to evade tax, 10% or $500 whichever is greater.

b) **Section 6485** — fraud or intent to evade deficiency determination, 25% of determination.

c) **Sections 6485.1 and 6514.1** — registration of a vehicle, vessel, or aircraft outside of this state for the purpose of evading tax, 50% of tax due.

d) **Section 6514** — fraud or intent to evade tax by failure to file return, 25% of tax, in addition to the mandatory Section 6511 failure to file penalty of 10%.

e) **Section 7155** — failure to obtain valid permit by due date of first return for the purpose of evading tax, 50% of tax due before permit obtained.

DEFINITION OF EVASION PENALTIES 0507.10

Fraud may be defined as conduct intended to deprive the State of tax legally due. An intent to evade may be defined as an intent to escape the tax through deception or misrepresentation. Although there may be a legal distinction between fraud and an intent to evade, the terms will be considered synonymous in this manual, and penalties imposed as a result of such act will be referred to as evasion penalties.

EVASION VS. NEGLIGENCE PENALTIES 0507.15

Evasion is a step beyond negligence. When negligence penalties are recommended, the facts should indicate that the taxpayer failed to exercise due care in keeping records or preparing returns or intentionally ignored certain duties or requirements. The evasion penalties are to be applied if it can be shown that the taxpayer not only failed to fulfill certain duties, but such failure was intentional and for the purpose of evading part or all of the true tax liability.

CONDITIONS WARRANTING AN EVASION PENALTY 0507.20

Before an evasion penalty can be imposed, there must be clear and convincing evidence that an existing tax deficiency is the result of a deliberate intent to evade payment. Where there is a substantial deficiency which cannot be explained satisfactorily as being due to an honest mistake or to negligence and where the only reasonable explanation is a willful attempt to evade payment, the 25% evasion penalty should apply. The size of the deficiency in relation to the tax reported should be taken into account. The indication that a deficiency is due to intent to evade increases in direct proportion to the ratio of understatement when it cannot otherwise be satisfactorily explained.

EVIDENCE OF EVASION 0507.25

It is very difficult to secure direct evidence that a taxpayer intended to evade a tax liability. In most cases, it is necessary to rely on circumstantial evidence. Certain acts are of such nature that they are evidence that a deliberate attempt has been made to evade payment of tax, and that an evasion penalty is warranted. Those commonly encountered include:

a) Falsified records, especially when more than one set is kept;

b) Substantial discrepancies between recorded amounts and reported amounts which cannot be explained;

c) Willful disregard of specific advice as to applicability of tax to certain transactions;

d) Failure to follow the requirements of the law, knowledge of which requirements is evidenced by permits or licenses held by taxpayer in prior periods ;

e) Tax properly charged, evidencing a knowledge of the requirements of the law, but not reported;

f) Transferring accumulated unreported tax from a tax accrual account to another income account.

Under the "clear and convincing" standard, any assertion of intent to evade the tax must be supported by as many of the above indicators as possible. These indicators of evasion must be documented. In addition to the findings of substantial discrepancies and proper charging of tax or tax reimbursement, other evidence of evasion must be included in the audit working papers. Such evidence can include copies of falsified records, Board letters providing specific advice, copies of previous permits and applications, and evidence of improper transfers of unreported tax. A summary of the evidence must be provided in the audit working papers. The summary must reference the schedules providing the evidence of evasion and must provide an explanation of how the evidence supports the recommendation for an evasion penalty.

BURDEN OF PROOF 0507.30

As a matter of law, fraud is never presumed but must be proven and the burden of proof is on the Board. However, the burden of proof is not beyond a reasonable doubt as in a criminal prosecution. (See *Helvering v. Mitchell* (1938) 303 U.S. 391). Instead, the standard of proof in civil tax fraud cases is "clear and convincing evidence" (*Renovizor's Inc. v. BOE* (9th Cir. 2002) 282 F.3d 1233). "Clear and convincing evidence" requires evidence so clear as to leave no substantial doubt as to the truth of an assertion of fraud. That is, there is a high probability that the assertion of fraud is true.

As noted in Sections 0507.20 and 0507.25, a taxpayer's intent to evade the tax is the key element to proving fraud. The mere fact that a taxpayer has a substantial tax liability does not in and of itself prove intent. Rather the evidence must support intent. For example, a consistent pattern of underreporting may indicate evasion, particularly if there is no other explanation for the understatement. However, additional evidence such as falsified records must be provided to support fraud when the underreporting is random. In all cases where a fraud penalty is recommended, the district administrator must submit evidence of a substantial nature that the taxpayer knowingly committed specific acts with the intention of defrauding the State of tax, which was legally due. (See Section 0507.75.)

EVASION BY AGENT, PARTNER OR EMPLOYEE 0507.40

Auditors should recommend the 25 percent penalty when a taxpayer's agent, partner, or employee has acted with intent to evade tax payment, even though such attempted evasion occurred without taxpayer's knowledge or consent. This is because the fraud of the agent is imputed to the principal except when the principal taxpayer is defrauded by the agent or employee. For example, when tax has been understated to cover up money or property stolen from the taxpayer, such an evasion will not be imputed to the taxpayer and the penalty should not apply. Generally, if a taxpayer has not benefited from the intent to evade, the evasion penalty should not apply.

AMOUNT TO WHICH PENALTY APPLIES 0507.45

The evasion penalties under sections 6485 and 6514 are imposed if any part of the deficiency is due to fraud or an intent to evade. Therefore the penalty will apply to the entire amount of the deficiency. In unusual cases where it appears inequitable to apply the penalty to an entire deficiency because, for example, a change in management during an audit period resulted in the discontinuance of fraudulent practices, or the reverse, field audit reports should be accompanied by *a full statement of the circumstances involved*, and separate Forms BOE–414–A should be submitted (although one Schedule 414–A2 will suffice). Headquarters will make two determinations, one with the penalty and one without.

Except for the penalties imposed under sections 6485 and 6514, evasion penalties should be applied only to the portion of the deficiency which was the result of the act or acts that constituted evasion.

KNOWINGLY OPERATING WITHOUT A PERMIT 0507.50

Section 7155 of the Sales and Use Tax Law imposes a 50% penalty of the tax due when a person *knowingly* fails to obtain a seller's permit. This penalty may be assessed when all of the following factors are present:

1. The taxpayer did not obtain a permit prior to the date the first tax return was due.
2. The taxpayer, while operating without a permit, knew a permit was required.
3. The average measure of tax liability during the period which the taxpayer operated without a permit was more than $1,000 per month.

In addition, the Section 7155 penalty may apply when a person is engaged in business at more than one location but knowingly fails to obtain a permit or subpermit for each location.

MISUSE OF A RESALE CERTIFICATE 0507.55

Section 6072 of the Sales and Use Tax Law imposes a penalty of 10% or $500, whichever is greater, for each transaction where a purchaser knowingly issues a resale certificate while the person is not actively engaged in business as a seller, for personal gain or to evade the payment of the tax. Section 6094.5 of the Sales and Use Tax Law imposes the same penalty, 10% or $500, whichever is greater, for each transaction where a purchaser knowingly gives a resale certificate for personal gain or to evade the payment of the tax, for property which he or she knows at the time of purchase will not be resold in the regular course of business.

When a resale certificate is accepted by a seller and it appears to meet all of the requirements of a valid resale certificate, it should be assumed the certificate was accepted in good faith. Unless there is other information that controverts this assumption, the seller should not be held liable for the tax Instead, the purchaser who knowingly issued an improper certificate will be pursued for the tax and penalty. If, however, it is disclosed that the seller makes a practice of accepting defective resale certificates, the seller's good faith is in doubt. In this case, tax should be asserted against the seller and a dual determination issued against the purchaser for the tax and penalty.

OUT OF STATE REGISTRATION OF VEHICLE, VESSEL OR AIRCRAFT 0507.60

Sections 6485.1 and 6514.1 provide a 50% penalty on a purchaser who registers a vehicle, vessel, or aircraft outside of California (i.e., in another state or foreign country) for the purpose of evading the tax. The standards of proof for this penalty are similar to those for fraud in general.

The penalty under sections 6485.1 and 6514.1 may not be asserted in conjunction with a penalty under section 7155 (failure to obtain a permit) or section 6485 or 6514 (fraud or intent to evade). However, this penalty may be asserted in conjunction with penalties under section 6511 (failure to file) or section 6072 or 6094.5 (misuse of resale certificate).

The penalty will generally be applicable when the purchaser is a California resident who purchased a vehicle, vessel, or aircraft for use in California and can provide no convincing evidence for registration out of state other than avoidance of the tax.

MULTIPLE PENALTIES 0507.65

Under certain circumstances, more than one penalty may apply to the same determination:

- The Section 6511 penalty (10% for failure to file return) should be applied along with a Section 6514 penalty (25% for fraud or intent to evade tax by failure to file return). A Section 6511 penalty may be applied with a Section 7155 penalty (50% for failure to obtain a permit) if appropriate.

However, an auditor should not impose two or more fraud or evasion penalties against the same determination when the penalties apply to the same series of acts or course of action:

- If a person with intent to evade tax fails to obtain a permit and fails to file a return, either the Section 7155 penalty (50% for failure to obtain a permit) or the Section 6514 penalty (25% for fraud or intent to evade tax by failure to file return) may be imposed, but not both.
- The Section 7155 penalty should not be applied in conjunction with a section 6485 penalty (25% for intent to evade).

The series of acts or course of action involved in the misuse of a resale certificate for purpose of evading payment of tax on **purchases** are different from those involved in failing to obtain a permit for the purpose of evading the tax on **sales.** Therefore the following penalties may apply to the same determination:

- A section 6511 penalty (10% for failure to file a return) may be applied with a section 6072 or 6094.5 penalty (improper use of resale certificate) since the 6511 penalty is not for fraud or intent to evade the tax. Similarly, the Section 7155 penalty (50% for failure to obtain a permit) may be added to the same determination if appropriate.

STATUTE OF LIMITATIONS FOR EVASION PENALTIES 0507.70

The application of evasion penalties can extend determinations beyond the otherwise applicable statute of limitations set forth in section 6487 (i.e., three or eight years). Therefore, tax can be assessed and penalties imposed for prior periods in which the taxpayer intentionally understated his or her tax liability. However, proof that the taxpayer intentionally understated his or her tax liability **within** the otherwise applicable statute of limitations (three or eight-years) is not by itself sufficient to support an evasion penalty for periods **outside** the statutory period. Ideally, evasion should not be asserted for periods outside the applicable statutory period (three or eight years), unless records for the outlawed periods are available, they establish an actual tax liability, and support the assertion of fraud.

Where audits have previously been made of prior periods and no evasion disclosed, such periods will not be included in subsequent audits even though evasion is discovered in periods covered by such subsequent audits unless there is a definite showing:

1. that evasion was present during the periods previously audited, and
2. that such evasion was not discovered at the time because information necessary to its detection was concealed from the auditors who made the previous audit, or because of some other act or fraud by the taxpayer.

APPROVAL OF EVASION PENALTIES 0507.75

In every instance where an evasion penalty is recommended, the audit report must be accompanied by a memorandum to the Program Planning Manager with an approval signed by the District Administrator. If the District Administrator is absent for an extended period the memorandum may be signed by the acting administrator. The memorandum must stand on its own and include in detail all of the facts and circumstances which are the basis for the evasion penalty recommendation. The facts and circumstances should be the same as those provided in the audit working papers and must cover any periods outside the statute of limitations. Any evidence that is not included in the audit working papers must be attached to the memorandum. If an audit includes related taxpayers, a separate memorandum must be prepared for each taxpayer on which the auditor recommends an evasion penalty. Approval to impose the evasion penalty will be obtained from the Program Planning Manager concurrently with the review process by the Centralized Review Section. After approval by the Program Planning Manager, the memorandum is returned to the district under a cover letter instructing the district to provide a copy of the approved memorandum to the taxpayer. *A copy of the memorandum may not be provided to the taxpayer or a representative until it is approved by the Program Planning Manager.*

MISCELLANEOUS 0508.00

FAILURE TO OBTAIN EVIDENCE THAT OPERATOR OF CATERING TRUCK HOLDS VALID SELLER'S PERMIT 0508.05

Any person making sales to an operator of a catering truck who has been required by the Board pursuant to section 6074 of the Sales and Use Tax Law to obtain evidence that the operator is the holder of a valid seller's permit issued pursuant to section 6067 of the Sales and Use Tax Law and who fails to comply with that requirement shall be liable for a penalty of five hundred dollars ($500) for each such failure to comply.

FAILURE OF RETAIL FLORIST TO OBTAIN PERMIT 0508.10

Any retail florist (including a mobile retail florist) who fails to obtain a seller's permit before engaging in or conducting business as a seller shall, in addition to any other applicable penalty, pay a penalty of five hundred dollars ($500). For purposes of this regulation, "mobile retail florist" means any retail florist who does not sell from a structure or retail shop, including, but not limited to, a florist who sells from a vehicle, pushcart, wagon, or other portable method, or who sells at a swap meet, flea market, or similar transient location. The term "retail florist" does not include any flower or ornamental plant grower who sells his or her own products.